September 1995

Audit of Subsidized Ancillary Services at The Nevada Test Site

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U.S. DEPARTMENT OF ENERGY
OFFICE OF INSPECTOR GENERAL

AUDIT OF SUBSIDIZED ANCILLARY SERVICES
AT THE NEVADA TEST SITE

Report Number: WR-B-95-08 Western Regional Audit Office
Date of Issue: September 8, 1995 Albuquerque, New Mexico 87185

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OFFICE OF INSPECTOR GENERAL
OFFICE OF AUDIT SERVICES

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SUMMARY

The Nevada Test Site became the nation's continental nuclear weapons test site in the early 1950s. During the first days of the nuclear test program, attracting the skilled labor force necessary to conduct the tests was difficult. The labor pool in Las Vegas was insufficient and workers had to be attracted from other locations. Additionally, an adequate amount of housing was not available in Las Vegas. Therefore, the Department established subsidized housing, food service, and transportation to entice and maintain a large, skilled workforce.

Since the mid-1980s, however, the Cold War ended, a moratorium on nuclear testing was put into effect, test site employment declined, and the test site's mission changed significantly. The purpose of the audit was to determine whether subsidies for the housing, food, and busing services were still necessary or reasonable.

The Department and its contractors have participated in at least six reviews since 1991 encompassing aspects of subsidies at the test site. Several of these reviews resulted in reports recommending reductions to the housing, food, and bus services. A strategic planning report completed in November 1994, for example, recommended closing certain food service facilities, increasing housing rates to fair market value, and studying a bus depot system. Other reports echoed the same themes. The Department should be credited for recognizing that actions should be taken to reduce subsidy costs. Moreover, the Acting Manager, Nevada Operations Office, has been proactive in reducing the busing subsidy by decreasing the number of buses and bus routes. The Acting Manager has also been fully supportive of the effort to further reduce subsidies. We appreciate these efforts.

Our audit showed, however, that additional opportunities existed to reduce costly subsidies for services that were not used extensively, that may no longer be needed, and that could be more fully supported by the users. The decline of a nuclear test program, reduced budgets, and a shrinking workforce have brought into question the need to heavily subsidize services that no longer directly support a national security mission. Thus, we

recommended that the Manager, DOE Nevada Operations Office, take steps to further reduce subsidies, including closing housing facilities or operating them on a break-even basis; operating the food services on a break-even basis; and, increasing the efficiency of the bus service. By implementing these recommendations, the Department could save \$10 million per year.

Management concurred with the spirit and intent of the recommendations and agreed to target full cost recovery for ancillary services. Management did not agree, however, with our presentation of the facts or the estimated annual savings. See Part III for management and auditor comments.

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PART I

APPROACH AND OVERVIEW

INTRODUCTION

During the Cold War, the Department developed and maintained an extensive infrastructure at the Nevada Test Site to facilitate the nuclear weapons test program. Subsidized housing service, food service, and busing service were an integral part of this infrastructure. The Department provided these subsidized services to attract and maintain a large force of skilled workers necessary to conduct nuclear tests. However, the Cold War has ended, a Presidential Directive in October 1992 placed a moratorium on nuclear testing, and test site employment is declining. Therefore, the audit assessed whether the subsidies for the housing, food, and busing services were necessary or reasonable.

SCOPE AND METHODOLOGY

The audit was conducted from January 1995 through April 1995, at the Nevada Operations Office and at the Nevada Test Site, located about 65 miles northwest of Las Vegas. Meetings were held with program officials from the Department contractors involved with the operation of the subsidized services.

To accomplish the audit objective, we:

- o reviewed contractual information;
- o reviewed union documentation;
- o reviewed financial data for Fiscal Years 1991-1994;
- o analyzed pricing and cost data for the three services;
- o analyzed usage statistics from January 1995 for the three services;
- o interviewed various Department and contractor personnel; and,
- o reviewed prior reports of other groups on the management of the program.

The audit was performed according to generally accepted Government auditing standards for performance audits and included tests of internal controls and compliance with laws and

regulations to the extent necessary to satisfy audit objectives. We limited the review of internal controls because the audit focused on the need and reasonableness of a specific program. Because the review was limited, it would not necessarily have disclosed all internal control deficiencies that may have existed at the time of our audit. We did not rely extensively on computer-processed data and, therefore, did not fully examine the reliability of that data. On March 7 and May 30, 1995, we met with the Acting Manager, Nevada Operations Office, to discuss the audit. An exit conference was held on August 10, 1995.

BACKGROUND

The Nevada Test Site became the nation's continental nuclear weapons test site on January 11, 1951. During the early days of the nuclear test program, it was difficult to attract the skilled labor necessary to conduct the tests. The labor pool in Las Vegas was insufficient and labor had to be attracted from other locations. Additionally, an adequate amount of housing was not available in Las Vegas. Therefore, the Department established subsidized housing, food service, and transportation to entice and maintain a large skilled workforce.

In addition, the Department also paid a daily allowance for "remote area pay" to test site employees. These payments were either \$5 or \$7.50 per day depending on where employees were stationed at the test site. From FY 1991 through FY 1994, total costs to the Department for remote area pay was about \$21 million. This was in addition to the costs for the subsidized services.

Nuclear testing continued through September 1992. A Presidential Decision Directive issued in that year stopped the testing but required the Department to conduct an experimental program and maintain a readiness posture, including a cadre of skilled workers, to resume nuclear testing within six months through Fiscal Year 1995. The directive further required that, beginning with Fiscal Year 1996, the Department maintain a 2- to 3-year readiness posture.

OBSERVATIONS AND CONCLUSIONS

Since 1991, the Department and its contractors have participated in at least six reviews encompassing aspects of subsidies at the test site. Several of these reviews resulted in reports recommending reductions to the housing, food, and bus services. A strategic planning report completed in November 1994, for example, recommended closing certain food service facilities, increasing housing rates to fair market value, and

studying a bus depot system. Other reports echoed the same themes.

The existence of these reports and their recommendations demonstrate that the Department was aware of the costly nature of the subsidies and the need to consider alternatives. In our March 7 meeting, in fact, the Acting Manager referred to the prior studies and expressed his desire to address the issues. The Department should be credited for recognizing that actions should be taken to reduce subsidy costs. Moreover, the Department has reduced the busing subsidy by decreasing the number of buses and bus routes. This action represents a positive step.

More opportunities to cut costs exist, however. Our audit showed that even after the moratorium on testing was put into place, the Department continued to pay costly subsidies for services that were not used extensively, that may no longer be needed, and that could be more fully supported by the users. The decline of a test program, reduced budgets, and a shrinking workforce have brought into question the need to heavily subsidize services that no longer directly support a national security mission. Thus, we recommended that the Manager, DOE Nevada Operations Office, take additional steps to reduce subsidies, including closing housing facilities or operating them on a break-even basis; operating the food services on a break-even basis; and, further increasing the efficiency of the bus service. By implementing these recommendations, the Department could save \$10 million per year.

Continuing to pay unreasonable subsidies is, in our opinion, a material internal control weakness that the Department should consider when preparing the yearend assurance memorandum on internal controls.

PART II

FINDING AND RECOMMENDATIONS

Subsidized Ancillary Services at the Nevada Test Site

FINDING

The National Performance Review recommended that federal agencies "cut back to basics" and not subsidize services that could be paid for by users. However, the Department continued to pay high subsidies for services that are not used extensively, that may no longer be needed, that could be more fully supported by the users, or that could be operated more efficiently. The Department has not seriously addressed the costs of these subsidies because of its interpretation of union contracts and continued adherence to over 30 years of past practices. Continuing these subsidies has cost the Department about \$31 million since the testing moratorium began at the end of Fiscal Year 1992 and will continue to cost about \$14 million per year.

RECOMMENDATIONS

We recommend that the Manager, DOE Nevada Operations Office, improve upon past practices by:

1. closing housing facilities at the Nevada Test Site or only maintaining a housing operation that is self-supporting and covers all costs of operating the facilities;
2. operating the food services on a break-even basis;
3. establishing a system-wide minimum occupancy level for bus services;
4. combining bus routes and stops to increase existing occupancy;
5. eliminating buses from the contract to maintain the established minimum occupancy level; and,
6. requiring the Chief Financial Officer to validate that the housing and food services are operating on a break-even or self-supporting basis.

MANAGEMENT REACTION

Management agreed with the spirit and intent of the recommendations and is working to implement subsidies costs savings, but did not agree with the portrayal of the facts and the potential savings. Detailed management and auditor comments are provided in Part III of this report.

DETAILS OF FINDING

The National Performance Review, completed in 1993, recommended that the Department of Energy redirect the mission of its nuclear testing facilities to meet post-Cold War national priorities. The Review also recommended that all federal agencies "cut back to basics" by eliminating spending on programs that are no longer needed and that serve special, not national, interests. Finally, the Review stated that the taxpayers should not be called upon to subsidize services that could be paid for more fully by users. The Department's strategic plan echoes a similar message by urging that its limited resources not be used to maintain past practices.

SUBSIDIZED ANCILLARY SERVICES

Our audit showed that the Department was maintaining past practices by continuing to subsidize services that are not used extensively and may no longer be needed, that could be more fully supported by the users of those services, or that could be operated more efficiently. As the following table illustrates, for the three services reviewed, the Department has continued to pay the difference between the costs incurred and the revenues generated, even though the test site's mission--nuclear testing--has been curtailed.

<u>Subsidized Services</u>			
<u>FYs 1991 - 1994</u>			
(in Millions)			
<u>Service</u>	<u>Costs</u>	<u>Revenues</u>	<u>Amount Subsidized</u>
Housing	\$ 7.4	\$ 3.1	\$ 4.3
Food	33.6	5.3	28.3
Busing	<u>38.9</u>	<u>3.4</u>	<u>35.5</u>
Totals	<u>\$79.9</u>	<u>\$11.8</u>	<u>\$68.1</u>

From FY 1991 through FY 1994, the Department spent \$68 million to subsidize these services, including about \$31 million since the testing moratorium began.

Housing Services

From FY 1991 through FY 1994, the Department spent about \$4.3 million to subsidize housing services. Our audit showed, however, that this subsidized housing is not being used extensively. The moratorium on nuclear testing has reduced the number of employees as well as their use of housing. The workforce at the test site, for example, has declined from 4,600 in FY 1991 to 3,100 in FY 1994. Of this reduced workforce, only about 14 percent (423/3100) used housing services during September 1994. Additionally, according to housing records, occupancy has dropped from an average of 46 percent in FY 1994 to about 36 percent in the first quarter of FY 1995. The moratorium on testing and the subsequent reduction in the number of employees combined with such low usage suggests that subsidized housing could be reduced and may not even be necessary.

In addition, we found that housing was no longer used as originally intended. When the Department was conducting nuclear tests, it provided employees with temporary quarters in order to meet work-related requirements. Thus, housing directly supported nuclear testing. The Department did not intend to provide workers with housing on a long-term basis or to provide housing merely for the convenience of employees. Our audit indicated, however, that the majority of occupants using the facilities rented them on a permanent basis. One day during the month of January, for example, out of the 494 occupants, 311 had rented their rooms on a permanent basis. Since nuclear testing was no longer occurring, there were no work-related requirements necessitating that employees spend the night or rent the rooms for indefinite periods. This situation led us to conclude that employees used these facilities for convenience and not for work-related requirements.

Even if housing were necessary to meet work requirements for nuclear testing, the cost of these services was not fully supported by the users. The rates charged to the users, for example, were unreasonably low. The daily rates ranged from \$.75 a bed (two beds per room) to \$10.00 for a private room. A majority of the beds (603 out of 1,074) rented for \$.75 per night. The audit showed that these low rates did not cover the cost of operations. In FY 1994, for instance, the costs associated with housing services totaled about \$1.6 million while the revenues generated totaled about \$560,000. Thus, the

Department had to subsidize housing services about \$1 million in FY 1994.

In addition to the normal operating costs, several facilities are currently being remodeled at a cost of \$370,000. These renovations are coming at a time when management is planning further reductions in the personnel who would use the housing and when the need for subsidized housing is not clearly essential to the test site's mission. The costs of these renovations are in addition to the amount the Department already subsidizes.

Food Services

Although the Department subsidized food services at the test site at a high cost (\$28.3 million FYs 1991 through 1994), other Department sites operated their food services at a significantly lower cost. In FY 1994, for example, Rocky Flats Field Office (Rocky Flats) subsidized a subcontractor about \$1.5 million to provide food service while the subcontractor at Lawrence Livermore National Laboratory (Livermore) operated the food service on a break-even basis. During the same time period, in contrast, the Department paid \$6 million to subsidize the food service at the test site. While the test site is the most remote location of the three, workers at all three locations face practical limitations in traveling offsite for meals.

One reason for the Department's high subsidy was that selling prices of the food at the test site were much lower than those at Rocky Flats and Livermore. For example, lunch at the test site consisting of cheeseburger, fries, and iced tea cost \$.90 compared to the costs of \$2.40 and \$3.55 for the same lunch at Rocky Flats and Livermore, respectively. While the selling prices of the food at the test site have remained low, the costs of running food service operations have increased. These low prices, in fact, did not cover the cost of the food. In FY 1994, for instance, the \$961,000 generated by food sales did not amount to the \$1.6 million spent on food supplies. The Department's subsidy, therefore, had to make up the difference between the revenues generated and the entire cost of the food services.

In addition, those costs which were identified as the subsidy amounts did not include other costs associated with operating the facilities, such as site maintenance. In FY 1994, for example, the cost of site maintenance for both food and housing services amounted to approximately \$700,000. Beginning in FY 1995, these services will be responsible not only for these costs but for the cost of fire protection and utilities as well.

Busing Service

From FY 1991 through FY 1994, the Department spent about \$35.5 million to provide bus transportation used by less than half the test site workers. On average, the bus records showed that approximately 44 percent (1350/3100) of the test site workforce used the bus service. The remaining 56 percent used either their private automobiles or government vehicles. Despite this low use, however, the Department continued to subsidize the bus service that previous reports described as inefficient.

Prior reports by the Department determined that the bus system could be operated more efficiently and recommended establishing a central bus depot in order to consolidate pick-up points. These reports showed that such a consolidation would reduce costs and increase operating efficiencies. The Department, however, did not implement this recommendation and has continued to subsidize an extensive and underutilized bus transportation service.

At the time of our audit, the bus service used 62 buses to service 62 routes with pick-up points throughout the metropolitan area and surrounding communities. Our analysis showed that the bus service provided multiple and overlapping pick-up points and provided service as far south as Boulder City. One intersection in Las Vegas, for instance, was serviced by four buses which left for the same general destination within one hour (5:00, 5:13, 5:15 and 5:52 AM). The audit also showed that buses typically had low occupancy. For example, buses designed to carry 47 passengers generally operated at less than 50 percent capacity. These three factors--low occupancy, an extensive route system, as well as numerous and overlapping pick-up points--indicate that the bus system could be operated more efficiently. As many as 30 buses, which cost about \$100,000 each per year to operate, could be eliminated.

CONTRACTS AND PAST PRACTICES

The Department has not seriously addressed the high costs of these subsidies because of its interpretation of union contracts and continued adherence to over 30 years of past practice. In discussions about possible reductions in the amounts paid in subsidies, administrative personnel have responded that the union contracts prohibit any changes to the services. However, our review of these contracts showed only three firm requirements. The Department is required to pay the remote area pay allowance of \$5 or \$7.50 per day and must provide bus service to the test site from the Las Vegas metropolitan area at an employee cost of \$1 each way. In addition, the union contract for the guards

requires that ample housing be made available. As of May 1, 1995, the number of guards at the test site has been reduced to about 82. At this time, the Department must provide housing for only this number of guards.

The Department has continued its past practice of maintaining low rates for housing and food services. In fact, the Department has held food prices at the 1962 levels even though revenues from food sales did not cover the cost of the food supplies. In addition, the Department has not implemented all of its own reports' recommendations to change housing or bus services; instead, it has adhered to past practices of occupancy for convenience and maintaining an extensive route system while its workforce continued to shrink.

Another reason for the Department's adhering to these practices was that, until recently, Defense Programs had supported much of the test site's infrastructure, including the three subsidized services reviewed. Even when nuclear testing was placed on hold and defense program dollars began to decrease, the Department continued paying large subsidies for housing and food services. In addition, it did not take appropriate steps to increase the efficiencies of the bus system.

SUBSIDY COSTS

By adhering to these past practices, the Department paid unreasonably high subsidies of about \$31 million in Fiscal Years 1993 and 1994. These subsidies will continue to cost about \$14 million annually. However, at least \$10 million of these annual costs could be eliminated by reducing services, passing more costs to the users, and operating the bus service more efficiently. By eliminating housing or by adjusting the rates to cover the costs of that service, the Department could save about \$1 million per year. Additionally, by requiring the food services to operate on a break-even basis, the Department could save an additional \$6 million per year; that is, the amount of the costs less the revenues for FY 1994. Finally, by establishing a range for minimum occupancy and a central pick-up point, the Department could reduce the number of buses needed as well as the extensive and overlapping services. For example, at 90 percent occupancy or about 42 people per bus, the Department could reduce the number of buses to about 32 (1350/42). This reduction of 30 buses could save the Department about \$3.0 million per year (\$100,000 per bus per year) or \$15 million over 5 years.

PART III

MANAGEMENT AND AUDITOR COMMENTS

In responding to our initial draft report, the Acting Manager concurred with the "spirit and intent" of the recommendations but did not agree with presentation of the facts or the estimated monetary impact. A summary of management's comments and our replies follows.

Subsidized Ancillary Services at the Nevada Test Site

Review Period and National Security

Management Comments. Management was concerned that by including Fiscal Years 1991 and 1992 in the scope of audit, the report failed to recognize that nuclear testing continued through September 1992. Management noted that a 1992 Presidential Decision Directive required the Department to conduct an experimental program and maintain a readiness posture including a cadre of skilled workers to resume nuclear testing within six months through Fiscal Year 1995. Beginning with Fiscal Year 1996, the Directive further required the Department to maintain a 2-3 year readiness posture. As a result, management noted, it would be inaccurate to assume there is no enduring stockpile stewardship mission or that events occurring in Fiscal Year 1993 could have had an influence on the financial data for Fiscal Years 1991-1992.

Auditor Comments. Fiscal Years 1991 and 1992 were included in the audit scope so that we could determine trends in the cost of subsidies. Management's comments on the Presidential Directive have been added to the report. The report neither states nor implies, however, that there is no longer a stockpile stewardship mission. Report conclusions are based, rather, on the fact that nuclear testing no longer occurs.

Costs of Subsidies and Estimated Savings

Management Comments. Management pointed out that the subsidies for housing, food, and busing have always been directly coupled with subsistence rates (remote area pay) under labor agreements. During the course of many negotiations, the Department has been successful in countering union demands for higher subsistence rates as a direct result of continued subsidies. Therefore, projected savings of \$10 million per year may not be attainable because of termination cost of leased buses and potential increase in the subsistence rates.

Auditor Comments. We recognize that some of the estimated \$10 million in savings could be offset if labor unions successfully negotiate for a higher subsistence rate. Our estimated savings of \$10 million per year assumes that the housing and food services would be operated on a break-even basis and that additional bus service efficiencies are achieved.

Cost Reduction Initiatives

Management Comments. Management stated that by combining subsidies over a four-year period (two of which included nuclear testing), the report fails to acknowledge the significant cost reduction initiatives already instituted by the Department. The report further incorrectly implies, according to management, that the Department instituted cost reduction activities only as a consequence of the OIG review. Management provided the following table to show that the annual cost of subsidies has been reduced by about \$2.6 million per year for FYs 1993 and 1994.

<u>Fiscal Year</u>	<u>Total Subsidies</u> (Millions)
FY 1991	\$17.9
FY 1992	\$19.3
FY 1993	\$16.7
FY 1994	\$14.1

The Department has recognized the need for further adjustments to these subsidies and is pursuing cost reduction initiatives within the constraints of the existing collective bargaining agreement and/or through appropriate renegotiations with the labor unions now scheduled for September 1995.

Auditor Comments. As noted earlier in the report, we are aware that the Acting Manager is concerned about subsidies and is taking action to reduce costs. This report presents additional opportunities for cost savings.

Housing

Management Comments. The report notes that only about 14 percent of the test site workforce used the housing services during September 1994. Management stated that the percentage of workforce using housing services does not have much bearing on the efficiency of the service and that the occupancy rate, which is a more representative performance measure, was about 43 percent in May 1995. The Department is currently reviewing the need for housing services, and as part of the renegotiation of the labor contracts scheduled for September 1995, the Department

expects to pursue raising the rates to achieve full-cost recovery.

Management also noted that \$370,000 being spent for housing remodeling includes replacement of damaged shower stalls, carpeting which could not be repaired, and other related activities. Even if the dorms were closed, the facilities would most likely be used as offices. The renovation costs would be required regardless of housing requirements.

Auditor Comments. The occupancy rates for FY 1994 and the first quarter of FY 1995 have been added to the report. Further, management's intended action to raise rates is responsive to our housing recommendation.

As for the remodeling, with current downsizing, there is, in our opinion, already adequate office space at the test site. Additionally, the majority of the \$370,000 was being spent on shower renovations, which would not be necessary for office space.

Food Services

Management Comments. Management believed that the comparison to Rocky Flats and Lawrence Livermore National Laboratory food services costs was fundamentally unsound. The test site is the only remote site in the comparison. While the Department is prepared to renegotiate the subsidies with the labor unions in September and will endeavor to achieve full-cost recovery, management believes subsistence will likely increase substantially if the subsidies are eliminated. Thus, the implication that all or a significant part of these subsidies can be saved is factually incorrect.

Auditor Comments. The comparisons are valid because workers at all three locations are restricted by time and distance from going to outside establishments for meals. The Department's intent to achieve full-cost recovery is responsive to our food service recommendation.

Busing Services

Management Comments. Management stated that, similar to the housing services, the percentage of the test site workforce which uses the busing services does not have much bearing on the efficiency of the service. A more representative performance measure would be the use rate. Since 1991, when there were 96 total bus routes, the Department has reduced the number of buses to 94, 82, and 63 in 1992, 1993, and 1994, respectively, to its

current number of 54 in 1995. (As noted earlier, there were 62 buses in service at the time of our fieldwork.) Management believes the report fails to acknowledge that significant progress has already been achieved and that the cost to reduce buses below the FY 1995 level will result in greater costs than to run the buses at the current usage level. The Department is, however, committed to exploring a central bus depot and to further reduce the number of buses as a consequence of formal contract renegotiations.

Auditor Comments. Managements actions to date are positive and its commitment to further reductions is responsive to our busing recommendations.

Summary

Although disagreeing, as noted above, with our presentation of facts and estimate of savings, management concurred with all recommendations. Nevada's specific action plan is to address all subsidy issues and target full cost recovery during contract negotiations scheduled for September 1995. Management's intended actions are responsive to the recommendations.

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